

X-7879

INTERPRETATION OF BANKING ACT OF 1933

(Copies to be sent to all Federal reserve banks)

April 28, 1934.

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Dear Sir:

This refers to your letter of October 9, 1933, addressed to the Board's General Counsel, in which you raise the question whether certificates of deposit which represent funds accumulated for bona fide thrift purposes and with respect to which a member bank merely reserves the right to require written notice of not less than 30 days may be classified as savings deposits within the meaning of that term as defined in the Board's Regulation Q. The Board regrets that due to the pressure of other urgent matters arising in connection with the Banking Act of 1933, it has not been able to complete its consideration of this question at an earlier date.

When Regulation Q was in process of formulation by the Federal Reserve Board, careful consideration was given to the question whether certificates of deposit with respect to which the bank merely reserves the right to require written notice of not less than 30 days might be classified as time deposits upon which interest may be paid; but, as stated in footnote 4 of the

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regulation, it is the Board's interpretation of the law that interest may not be paid on such a certificate of deposit, because it is in fact payable on demand unless prior to such payment notice of not less than 30 days is actually required, and because the prohibition in the law upon payment by a member bank of any time deposit before its maturity clearly contemplates that time deposits (other than savings deposits) upon which interest is payable must have a definite maturity for at least 30 days prior to payment. Accordingly, such a certificate of deposit upon which the bank merely reserves the right to require written notice of not less than 30 days may not be classified as a time deposit within the meaning of Regulation Q.

You call attention, however, to the fact that one of the requirements of the definition of savings deposits in Regulation Q is that "the passbook or other form of receipt" evidencing such a deposit must be presented to the bank whenever a withdrawal is made, and the question arises whether a certificate of the kind described may constitute a "form of receipt" within the meaning of this requirement so that deposits represented thereby may be considered savings deposits. In this connection it is noted that you indicate that the certificates in question are in effect payable on demand upon the surrender of the certificates duly endorsed.

Section 19 of the Federal Reserve Act provides that no

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time deposit may be paid before its maturity by a member bank, whereas the payment of savings deposits without requiring notice of withdrawal is under certain conditions permissible under the law. In order to carry out the intention of the statute in this connection it is believed important that neither the law nor the Board's regulation should be so interpreted as to encourage or facilitate evasions of the prohibition upon the payment of time deposits before their maturity or the prohibition upon the payment of interest on deposits payable on demand. A certificate of deposit, as that term is generally understood, is an instrument evidencing the receipt of a single amount on deposit the entire amount of which will be repaid at one time and only upon the surrender of the certificate. Savings deposits, on the other hand, are received under continuing contracts covering deposits made from time to time, from which withdrawals may be permitted from time to time, all of which are evidenced by a single form of receipt which must be presented but need not be surrendered whenever a withdrawal is made. There is thus an essential distinction between certificates of deposit and receipts for savings deposits within the commonly accepted meaning of these terms and the Board feels that the preservation of this distinction is necessary in order to carry out the purposes of the statute. Accordingly, the phrase "other form of receipt" as used in the definition of savings

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deposits in the Board's Regulation Q is not to be interpreted as including a certificate of deposit which by its terms contemplates that only one deposit will be evidenced thereby and that the entire amount will be repaid upon the surrender of the certificate. The phrase in question in Regulation Q recognizes the fact that in some circumstances banks may find it desirable to issue receipts for savings deposits which are not in the usual form of savings pass books; but it is the intention of the regulation that every such receipt for savings deposits should be a contract of a continuing character evidencing deposits the amount of which may be increased or decreased from time to time without the necessity of surrendering the receipt or issuing another such receipt.

The Federal Reserve Board, accordingly, suggests that member banks take steps to exchange or substitute savings pass books or other receipts which comply with the intention of the regulation as discussed above for certificates of deposit outstanding which are subject merely to the right of the bank to require notice of not less than thirty days, in order that interest may be paid on deposits represented thereby. In view of the fact, however, that this matter has been pending before the Federal Reserve Board for a decision for several months, the Board will not object to the payment of interest on deposits represented by such outstanding certificates covering funds accumulated for bona fide

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thrift purposes until such time as such exchange or substitution can be brought about in an orderly manner after reasonable notice has been given by the bank to the holders of such certificates.

Very truly yours,

(Signed) Chester Morrill.

Chester Morrill,
Secretary.